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TAGS: [MASS](#) [MARR](#) [MCAP](#) [ECON](#) [PGOV](#) [PINR](#) [PREL](#) [SI](#)
SUBJECT: U.S. FIRMS STRUGGLE TO COMPETE AS DEFENSE
ACQUISITIONS GROW CLOUDIER IN SLOVENIA

REF: 06 LJUBLJANA 388

Classified By: COM Thomas B. Robertson for reasons 1.4 (b) and (d)

¶1. (S) Summary. Nearly one year after the Slovenian Ministry of Defense (MOD) announced that Finnish defense contractor Patria won a 330 million USD (263 million Euro) contract to supply 135 8x8 armored vehicles to the GoS, the issue continues to dominate headlines amid allegations of cost overruns and non-transparency in the selection process. Opposition leaders forced a special session of Parliament in February and succeeded in gaining parliamentary authorization in March for an inquiry commission to review the purchase. The government coalition responded by creating a similar commission in April to review all defense purchases, including those made when the current opposition parties ran the government. With dueling parliamentary investigations up and running and October 2008 parliamentary elections coming slowly into view, questions surrounding Slovenia's largest defense purchase in the 15 years since independence grow increasingly aggressive. More troubling yet, the purchase is just the most prominent example of a defense acquisition process that is opaque, political, and increasingly inhospitable to U.S. firms. While Slovenian military contacts continue a close and cordial relationship with their U.S. interlocutors at all levels, it is increasingly apparent that political influence from above is guiding the hands of officials making acquisition decisions. End Summary.

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ARMORED VEHICLE PURCHASE PLODS FORWARD AMID CONTROVERSY
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¶2. (C) Since the Slovenian Ministry of Defense's (MOD) announcement on June 12, 2006 that Finnish defense contractor Patria won a 330 million USD (263 million Euro) contract to supply 135 8x8 armored vehicles to the GoS (reftel), post has followed months of simmering allegations beginning with complaints of non-transparency in the tender review and selection process, talk of significant cost discrepancies between the tender amount and what the GoS would eventually

pay, disputes about how the quality of the two competing vehicles and the overall bids were compared, and allegations that (in a cost cutting maneuver) the contract allows for the delivery of vehicles that are not properly equipped.

¶3. (C) Given that the losing (and only other) bidder in the controversial tender was a company with U.S. interest -- Slovenian defense company Sistemska Tehnika (ST), which is 70 percent owned by Slovenia-based Viator & Vektor (V&V) and 12.7 percent owned by Austria-based Steyr-Daimler-Puch, which, in turn, is a wholly-owned subsidiary of the General Dynamics (GD) corporation -- COM has repeatedly raised concerns about the transparency and efficacy of the GoS,s 8X8 deal with Patria (as well as other defense acquisition tenders involving U.S. bidders) at the highest level including Prime Minister Janez Jansa (June and December), and both former and current Chiefs of Defense Ladislav Lipic (June) and Albin Gutman (July and November).

¶4. (C) Dozens of front-page newspaper articles, political cartoons, and opinion pieces questioned the GoS's choice of Patria. Events held by the losing bidder ST to formally present its armored vehicle 8x8 -- the Krpan -- in manufacturing site Ravne na Koroskem and in Ljubljana further fueled the fire in mid-October, and resulted in a print advertising campaign from Patria -- the first time Slovenia has seen a public advertising campaign for weapons and military equipment -- calling the Krpan into question.

¶5. (SBU) "Tough and merciless" negotiations (as described by Slovenian press) between the MOD and representatives of Patria and its local partner, Rotis, to sign a formal contract dragged on for over six months (from June 12 to December 19) before the parties agreed on costs, offsets, and

the inclusion of Slovenian industry in the vehicles, production. But signing the paperwork put to rest only one part of the controversy.

¶6. (SBU) Another issue was the ongoing debate about where the Patria 8x8 will be built in Slovenia, with losing bidder ST owning the only active military vehicle assembly plant in the country (in Ravne na Koroskem). Patria's local representative Rotis said that Slovenian home appliance manufacturer Gorenje (the lead subcontractor for the Patria deal despite its lack of a military branch) would ultimately be the manufacturer and assembler of the vehicles. Media reports in December highlighted rumors that ST owners Viator & Vektor (and its parent company General Dynamics) are considering selling ST or simply the assembly plant in Ravne na Koroskem to Gorenje, given that ST no longer has an interest in the production of 8x8 vehicles in Slovenia. The move would effectively allow production in the same plant by the same workers as the ST bid called for, but under ownership of the preferred bidder. Gorenje leadership said that acquiring ST was not in its plans, however the General Manager of Rotis Ivan Crnkovic said, in media interviews, that it would be a "winning formula for the Slovenian economy." On January 31 Gorenje announced that it would build parts and assemble the vehicles at a Gorenje facility in the town of Sostanj, though Gorenje CEO Franjo Bobinac told media that Gorenje would not exclude the possibility of cooperation with other Slovenian companies, including ST. Media reports April 19 said that Gorenje had received building permits for a 9,000 square meter plant in Sostanj that would be operational by fall 2007, with the first Slovenian-produced Patria armored vehicle coming out sometime in 2008. ST's new general manager announced February 20 that the company would split into two units, one military and one civilian, with the bulk of ST's future interests coming from the latter's production of consumer products. There has been no further decision on the future of ST's Ravne na Koroskem military vehicle assembly plant.

17. (C) Opposition leaders strongly stepped up criticism of the 8x8 armored vehicles purchase this spring calling an extraordinary session of Parliament on February 15 to discuss the matter. The chief target of criticism continues to be Minister of Defense Karl Erjavec though he has steadfastly fought back critics and, thus far has withstood rumors that the deal will ultimately lead to his departure from the MOD. In a press conference called to respond to the move for an extraordinary session of Parliament, Erjavec reiterated that the deal was in conformity with the tender and the rules, that legislation allows members of Parliament to look at documents from the MOD, but that they must protect business secrets, that the whole episode is a political smear from the

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opposition parties, and that the media is to blame for stoking the fire of the controversy. Before the session took place, the Parliamentary Defense Committee rejected every resolution opposition members had hoped to pass, including ones that said that Minister of Defense Karl Erjavec had knowingly misled the public about the price of the vehicle purchase and another that said the purchase was harmful to Slovenia. The actual session was a highly politicized back-and-forth with opposition leaders repeating their criticisms of the deal and government coalition leaders, including Erjavec, refuting the criticism and highlighting the purchase's benefits for the Slovenian economy and for Slovenia's ability to contribute to NATO. Several members of Parliament said the purchase was a return to past practices, and that non-transparent, even corrupt, practices were a regular occurrence throughout the history of the MOD. They also seized on the fact that the director of Patria's local partner, Rotis, was an aide to Prime Minister Janez Jansa when he was the Minister of Defense.

18. (SBU) March 30, opposition leaders succeeded in getting Parliamentary approval for an inquiry commission to look into the purchase. Specifically, it is charged with determining if the tender for the vehicle purchase favored any particular bidder, what the exact details are for the purchase, and to investigate the responsibility of public officeholders in hindering oversight of the MOD and the Slovenian Armed Forces. The coalition failed to expand the inquiry more generally to defense acquisitions, and thus decided to pursue a second inquiry commission to look at defense acquisitions deals in Slovenia from 1994 to 2007 (including the purchase of 6x6 armored vehicles, 155mm Howitzers, Pilatus turbo prop airplanes and a government jet, as well as the refurbishment of T-55 tanks) during the majority of which the current center-left opposition parties held the government. The inquiry commissions were formally established in late April and began work in May. They have yet to release any official findings and have no official deadlines.

GOS TALKING POINTS: PATRIA DEAL FAIR AND TRANSPARENT

19. (S/NF) Publicly and in official meetings with the COM and EmbOffs, government officials including Gutman and Jansa have consistently used one set of talking points, stating that it will stick with the Patria bid, that the Patria bid was superior in all areas of review (quality of product, cost, and commercial impact), that Sistemska Tehnika's bid was clearly inferior, that ST's poor performance was a result of poor preparation and overconfidence that it would secure the deal, and that the entire tender process was "by the book." One notable exception was the (now retired) Commander of the Training and Doctrine Command, Brigadier Jozef Zunkovic (strictly protect), who privately told ODC Chief June 22 that the decision had been "political" and that the Patria was "not the vehicle we (i.e. the military) wanted." Other senior SAF leaders close to the Embassy, including the generally affable and open Deputy Chief of Defense Alojz Steiner and former Chief of Defense Ladislav Lipic have been particularly tight lipped about the decision.

¶10. (S/NF) In a December conversation with Jansa, COM asked about rumored forty percent cost overruns on the Patria deal and commentary that the GOS would have to do without key elements of the vehicle (including floatability and radio encryption) or reduce the number of vehicles purchased to meet the original cost limitations. Jansa demurred and claimed not to have any information on the issue, saying that the issue was in Erjavec's portfolio and that it was his job to make sure everything transpired in a transparent matter.

ANTI-U.S. PERSPECTIVE GROWING AT THE MOD?

¶11. (C) The decision to purchase Patria's armored vehicles are only the most prominent example of the negative recent experiences of USG corporations competing for open defense contracts from the GOS. In spring 2007, U.S.-based Cubic Corporation lost a two way competition to provide a tactical engagement simulation system as part of a broader combat training center project that is being heavily supported by the Embassy's Office of Defense Cooperation. Post strongly advocated for the MOD to consider the benefits of purchasing from Cubic (via Foreign Military Sales) in order to ensure future training interoperability with U.S. forces and given Cubic's overwhelming role as the leader in this market. The USD 7 million contract was awarded to Swedish firm Saab in a deal that Embassy contacts have also identified as non-transparent and corrupt. EmbOffs have also heard that the SAF are looking at alternatives for even the most basic defense purchases, including spare parts and maintenance for SAF Hummers.

¶12. (S/NF) This seeming push away from American defense corporations came in line with the strange appointment of Marjan Senica to the post of Director General of the Directorate of Logistics (which also handles acquisitions) at the MOD in mid-2006. Senica was previously the director of Slovenian corporation STO-Ravne, but was dismissed in 2002, after pressure from Embassy officials, because of his direct involvement in efforts to export military goods from Slovenia to Syria. After a brief time in the position (during which the Patria deal was made), Senica moved to the deputy position in the directorate. Embassy contacts say that Senica is pushing a generally "anything but American" ideology into the acquisitions office at the MOD.

COMMENT

¶13. (S/NF) Over the past year, post has closely followed allegations from mainstream media, political pundits, and internal and external observers of the MOD, with all parties reporting that the selection and negotiation process used by the MOD in the acquisition of the 8x8 armored vehicles was faulty. At best, the selection and negotiation processes have lacked transparency, with the public still not receiving a detailed account of how GoS money is being spent, and what it is getting in return. At worst, industry insiders tell us they suspect criminal actions, including bribes and major political party payoffs, in exchange for the lucrative contract. Some have even suggested the vehicle purchase was a conduit for the filling of campaign coffers in advance of the first big test of the ruling coalition, parliamentary elections in 2008.

¶14. (S/NF) According to a clandestine source with direct access to an employee of Rotis, Prime Minister Jansa's SDS received more than 2.8 million Euro from Patria "under the table" as part of the deal for armored vehicles. The source also noted that Sto Ravne had failed to offer a similar contribution to Jansa's party.

¶15. (S) Given the smallness of Slovenia, the familiar cast of characters surrounding the controversy is not all that

surprising. Nor is the fact that a "smoking gun" has not emerged because of Slovenia's complete lack of investigative reporting. How the controversy will play out now that parliamentarians are on the case remains to be seen. What is certain is that the political knives are out, and it is possible that this controversial defense deal may be the fight that frames the next few years of Slovenian politics.

¶16. (S) Another consideration is Slovenian interest in furthering its ties in Europe and cementing itself into the European military industrial complex. While Slovenian military contacts continue a close and cordial relationship with their U.S. interlocutors at all levels, it is possible that MOD leaders do not see "buying American" as particularly valuable in further enhancing the bilateral relationship. The decision to go with Finnish Patria was hailed by the Finns and was politically useful for a government that wants to burnish its credibility as the first among the newest members of the EU. While the GOS urgently prepares to take the helm of the European Union in January, the very "Balkan" story of its defense acquisitions process reminds us that while Slovenia has come very far, there is still a ways to go.

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